Gold Stocks Surge After Fed Rate Hike: What Gives?

Description

Mr. Market served up another one of his odd surprises March 15 when gold rallied after the U.S. Federal Reserve raised its target interest rate.

Why is this odd?

The normal expectation in the market is that rising rates are bad news for gold.

Higher interest rates tend to increase the opportunity cost of holding non-yielding assets such as gold. Rising rates in the United States can also put upward pressure on the value of the American dollar, in which gold is priced, making the metal more expensive for holders of other currencies.

So, what happened?

Leading up to the rate decision, the market had pretty much accepted that the Fed was going to bump up the rate. Gold and gold stocks sold off over the past few weeks in anticipation of the move, and the focus was more on whether or not the Fed would indicate that it might move more aggressively than expected.

In fact, rumours had started to circulate that the Fed could signal intentions to raise rates four times this year instead of three. That would have been negative for the precious metals.

When the announcement finally came out, the Fed stayed the course on its previous outlook, indicating three hikes are on the table, and that triggered a relief rally in gold.

In the market, bad news can be good news when you are expecting really bad news.

What's next for the gold market?

Now that the rate question is more or less sorted out, the market will likely turn its focus back on other situations that might trigger a move into safe-haven assets.

President Trump continues to take a hard line with key trading partners, especially China. If the rhetoric continues along the same lines, the market could start to worry about a full-blown trade war.

Europe is also a potential source for market chaos. Brexit might get ugly, and the election in France could produce a new president who wants to dump the euro and hold a referendum on E.U. membership.

At the same time, Italy’s banks are a mess and continue to threaten the broader European banking system.

Of course, the markets could simply ignore any shocks, as happened after last year’s Brexit vote, but there is potential for a flight into gold if fear and uncertainty starts to take hold.

Which stock should you buy?

If you think precious metals are at the beginning of a longer-term recovery, **Barrick Gold Corp.** (TSX:ABX)(NYSE:ABX) is probably a good stock to watch.

The company is the world’s largest gold producer and has improved its operating efficiency to the point where all-in sustaining costs are among the lowest in the industry. The business is generating strong free cash flow at current prices, and Barrick even raised its dividend when the Q4 2016 results came out.

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